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PREVALIDATION OF INTERGOVERNMENTAL TRANSACTIONS

Report No. D-2001-135

June 6, 2001

Office of the Inspector General
Department of Defense

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Acronyms

DFAS	Defense Finance and Accounting Service
GAO	General Accounting Office
OPAC	On-Line Payment and Collection



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-4704

June 6, 2001

MEMORANDUM FOR DIRECTOR, DEFENSE FINANCE AND ACCOUNTING
SERVICE

SUBJECT: Audit Report on Prevalidation of Intergovernmental Transactions
(Report No. D-2001-135)

We are providing this report for review and comment. The Director, Defense Finance and Accounting Service, did not respond to the draft report. We performed the audit in response to an allegation made to the Defense Hotline.

DoD Directive 7650.3 requires that all recommendations be resolved promptly. Therefore, we request that the Director, Defense Finance and Accounting Service, provide comments on the recommendation by July 6, 2001.

We appreciate the courtesies extended to the audit staff. Questions on the audit should be directed to Mr. Richard B. Bird at (703) 604-9159 (DSN 664-9159) (rbird@dodig.osd.mil) or Mr. Carmelo G. Ventimiglia at (317) 510-3852 (DSN 699-3852) (cventimiglia@dodig.osd.mil). See Appendix D for the report distribution. The audit team members are listed inside the back cover.

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Report No. D-2001-135

(Project No. D2000FI-0250)

June 6, 2001

Prevalidation of Intergovernmental Transactions

Executive Summary

Introduction. The audit was performed in response to an allegation to the Defense Hotline. The complainant alleged that Defense Finance and Accounting Service Norfolk stopped prevalidating payments for naval shipyards based on guidance from Defense Finance and Accounting Service Arlington.* The prevalidation of payments requires the matching of disbursements to corresponding obligations in the official accounting records before the actual payment is made. Payments that are not prevalidated may result in improper payments.

Intergovernmental transactions result when one Federal agency makes payments to another Federal agency or makes a payment on behalf of another Federal agency and requests reimbursement for such payment. The Department of the Treasury's On-Line Payment and Collection system is a standardized billing, transfer, and adjustment process for processing intergovernmental transactions. Clearing accounts temporarily hold collections or disbursements pending identification of the transactions to the applicable receipt or expenditure budgetary account. A suspense account is a type of clearing account.

Objective. The audit objective was to evaluate the process for prevalidating payments for naval shipyards. The review of the management control program as it related to making vendor payments will be conducted as part of an ongoing audit of controls over the Computerized Accounts Payable System.

Results. We did not substantiate the allegation that Defense Finance and Accounting Service Norfolk stopped prevalidating payments for naval shipyards. Defense Finance and Accounting Service Norfolk prevalidated commercial payments for naval shipyards. However, Defense Finance and Accounting Service Norfolk transferred the payment of certain intergovernmental transactions to the On-Line Payment and Collection system, which never had a program for prevalidating payments. The change occurred as follows.

- Prior to mid-1999, intergovernmental transactions were prevalidated similar to commercial payments.

*DFAS Arlington is the site of DFAS headquarters.

- In mid-1999, the Department of the Treasury's On-Line Payment and Collection system was used to process most intergovernmental transactions. As part of that process, Defense Finance and Accounting Service Norfolk performed detailed reviews of the support for charges to funds of the naval shipyards by other governmental organizations before posting them to accounting records, but after the payments were made.
- In June 2000, Defense Finance and Accounting Service Norfolk discontinued performing detailed reviews of the support for On-Line Payment and Collection transactions before posting them to accounting records. Defense Finance and Accounting Service Norfolk stopped performing the detailed reviews because the Department of the Treasury issued new reporting procedures for unprocessed transactions between Federal agencies and the process was time-consuming.

The Defense Finance and Accounting Service had not implemented a program to prevalidate On-Line Payment and Collection transactions and did not report amounts in suspense account F3885, Undistributed Intergovernmental Payments, as unmatched disbursements. As of September 30, 2000, the dollar value of payments in suspense account F3885, over 90 days old, was \$471 million. As a result, On-Line Payment and Collection transactions were not properly reviewed before payment and the dollar value of unmatched disbursements for DoD was understated in Problem Disbursement Reports. For details of the audit results, see the Finding section of the report.

Summary of Recommendations. We recommend that the Director, Defense Finance and Accounting Service, develop a plan for prevalidating intergovernmental transactions. The plan should identify specific milestones, performance measures, and expected backlogs.

Management Comments. The draft report was issued on March 14, 2001, and no management comments were received. We request that the Director, Defense Finance and Accounting Service, provide written comments on this report by July 6, 2001.

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Background

Allegation. The audit was performed in response to an allegation to the Defense Hotline. The complainant alleged that Defense Finance and Accounting Service (DFAS) Norfolk stopped prevalidating payments for naval shipyards based on guidance from DFAS Arlington.* The complainant stated that by not prevalidating payments, overpayments would occur and individuals and contractors would bill the Government for goods and services not provided. The specific allegation is addressed in Appendix C.

Prevalidation. Disbursements must be matched with corresponding obligations in official accounting records to ensure that funds are spent in accordance with the purposes and limitations set by Congress and to avoid fraudulent disbursements or erroneous payments. Before a disbursement is made, disbursing officials should ascertain that each line of accounting to be charged represents a valid obligation. The matching of disbursements to corresponding obligations in accounting records prior to payment is known as prevalidation. The prevalidation process is essential when one organization disburses funds that are accounted for by a different organization. By prevalidating payments, DFAS should reduce unmatched disbursements and ensure the proper accounting for DoD payments. A disbursement transaction that has been received and accepted by an accounting station, but has not been matched to the correct obligation, is considered an unmatched disbursement.

DFAS Norfolk disburses funds to contractors as commercial payments and makes intergovernmental payments to other Federal agencies. DFAS Norfolk also accounts for commercial and intergovernmental payments made for the Norfolk Naval Shipyard, Norfolk, Virginia; the Puget Sound Naval Shipyard, Bremerton, Washington; and Portsmouth Naval Shipyard, Portsmouth, New Hampshire.

On-Line Payment and Collection Transactions. Disbursements may be made via the On-Line Payment and Collection (OPAC) system. The Department of the Treasury's OPAC system is a standardized interagency billing, transfer, and adjustment process that operates via a telecommunications network. It simultaneously bills and collects intergovernmental transactions between Federal agencies. In FY 2000, the net amount of OPAC payments and collections (OPAC transactions) made by DoD disbursing stations totaled about \$26.8 billion.

DFAS Norfolk used the OPAC system to process transactions with other Federal agencies and to transfer funds between DFAS activities. When one Federal agency charges another for work, the billing agency receives credit via a transfer of funds process through the Department of the Treasury. An OPAC disbursement transaction should be matched to its corresponding obligation or recorded against its proper expenditure account by the fund holder's accounting station.

*DFAS Arlington is the site of DFAS headquarters.

Objective

The audit objective was to evaluate the process for prevalidating payments for naval shipyards. The review of the management control program as it related to making vendor payments will be conducted as part of an ongoing audit of controls over the Computerized Accounts Payable System.

Prevalidating Intergovernmental Transactions

We did not substantiate the allegation that DFAS Norfolk stopped prevalidating OPAC transactions for naval shipyards. DFAS Norfolk prevalidated commercial payments for naval shipyards. However, DFAS Norfolk did not prevalidate intergovernmental transactions once the OPAC system was used for payment. DFAS did not prevalidate OPAC transactions, and most other intergovernmental transactions, because automated systems did not exist to systematically prevalidate them. DFAS was reluctant to manually prevalidate intergovernmental transactions because it would be time-consuming. DFAS also did not report amounts in suspense account F3885, Undistributed Intergovernmental Payments, as unmatched disbursements until DoD policy changed. As of September 30, 2000, the dollar value of payments in suspense account F3885, over 90 days old, was \$471 million. As a result, OPAC transactions were not properly reviewed before payment and the dollar value of unmatched disbursements for DoD was understated in Problem Disbursement Reports.

Prevalidation Plans

DFAS prepared a plan in February 1995 for prevalidating disbursements in response to the Department of Defense Appropriations Act, FY 1995 (Public Law 103-335, section 8137). The plan focused on prevalidating payments to commercial contractors and vendors. The plan recognized the need to prevalidate other types of payments, such as transfers between appropriations and other reimbursements. However, the plan did not consider transfers between appropriations and other reimbursements as disbursements because there was not a reduction of funds in the Department of the Treasury.

Review of Prevalidation Plans

In Inspector General, DoD, Report No. 96-156, "DoD Plan to Match Disbursements to Obligations Prior to Payment," June 11, 1996, we recommended that payments such as transfers between appropriations and other reimbursements be prevalidated. On October 21, 1996, the Deputy Chief Financial Officer agreed with the need to prevalidate other types of payments. However, he stated that prevalidation of these payments would increase significantly the volume of transactions requiring prevalidation and would require numerous system changes. In the meantime, any manual effort to implement this change without adversely affecting the Department's ability to pay its bills in a timely manner would require a much greater commitment of personnel resources. Therefore, the Deputy Chief Financial Officer stated that the Department would prevalidate other types of payments, such as transfers between appropriations and other reimbursements, as migratory systems become operational with the capacity to accommodate the prevalidation requirements for

these payments. The long-term goal of DoD is to have a single shared database that is updated and accessed by expert functional systems. In the interim, efforts to prevalidate transactions would be undertaken where feasible and cost-effective.

DoD prepared two additional plans in 1997 in response to Senate Report No. 104-286, which accompanied the Department of Defense Appropriations Act for FY 1997 (Public Law 104-208). However, neither plan addressed the need to prevalidate transfers between appropriations and other reimbursements.

Need to Expand Prevalidation Requirements

DFAS has not updated the prevalidation plans since they were issued; however, DFAS has lowered the dollar threshold for prevalidating contract and vendor payments. Beginning November 1, 2000, the prevalidation threshold for all Mechanization of Contract Administration Services system contracts was \$100,000. The threshold was to be incrementally lowered in 2001. Most payments made using vendor payment systems were to be prevalidated at zero dollars. The prevalidation process occurred either through automated system interfaces or manually when automated system interfaces did not exist to systematically prevalidate transactions. DoD continued to be reluctant to manually prevalidate transactions. Some system enhancements have been made to automatically prevalidate payments. For example, Navy Working Capital Fund activities prevalidate reimbursable transactions in the Standard Accounting and Reporting System – Headquarters Module. However, OPAC transactions were not prevalidated and DFAS has not implemented a program to prevalidate them. Consequently, these transactions may result in unmatched disbursements that need to be researched and resolved after payment.

Suspense Account F3885

OPAC transactions in suspense account F3885, Undistributed Intergovernmental Payments, were not reported as unmatched disbursements even though they had not been properly matched to detail obligations in accounting records. DoD did not require amounts in suspense accounts to be reported as unmatched disbursements until DoD Regulation 7000.14-R, “DoD Financial Management Regulation,” volume 3, chapter 11, “Unmatched Disbursements, Negative Unliquidated Obligations, In-Transit Disbursements, and Suspense Accounts,” was revised in January 2001. The revised guidance contained procedures that required each intergovernmental disbursement (other than an interfund transaction) recorded in account F3885 to be transferred to its proper expenditure account within 60 days. If the intergovernmental disbursement transactions were not transferred to their proper expenditure accounts within 60 days, the accounting station would be required to record the disbursement transactions as unmatched disbursements. Each interfund disbursement transaction recorded in account F3885 was to be transferred to its proper

expenditure account within 6 months. All transactions in account F3885 made on or after January 1, 2001, were to be reported in accordance with these procedures.

When the fund holder's accounting station receives a disbursement transaction that contains an invalid or incorrect fund citation, the accounting station should record the disbursement transaction in account F3885, while the transaction is under research. These transactions are to be researched and resolved before they are properly matched in accounting records. Generally, a transaction should not remain in suspense account F3885 for more than 60 days. At fiscal year's end, the DFAS central accounting sites apportion and distribute the year-end balances in account F3885 to the predominant appropriation accounts for reporting to the Department of the Treasury.

DFAS central accounting sites submitted monthly reports to DFAS Arlington on problem disbursements (unmatched disbursements and negative unliquidated obligations). The DFAS central accounting sites also identified the dollar value of suspense account balances in specific aging categories. However, the dollar values of transactions in suspense accounts were not reported as unmatched disbursements even though the transactions had not been properly posted in accounting records. Implementation of the procedures in DoD Financial Management Regulation, volume 3, chapter 11, should result in the appropriate classification and reporting of transactions in suspense accounts as unmatched disbursements.

A category for reporting suspense account transactions that were more than 60 days old was not established. However, the dollar value of transactions more than 90 days old was reported. As of September 30, 2000, the dollar value of payments in suspense account F3885 that were more than 90 days old totaled about \$471 million.

Conclusion

We did not substantiate the allegation that DFAS Norfolk stopped prevalidating OPAC transactions for naval shipyards. DFAS Norfolk prevalidated commercial payments for naval shipyards. However, DFAS Norfolk did not prevalidate payments once the OPAC system was used to process intergovernmental transactions. DFAS did not prevalidate OPAC transactions, and most other intergovernmental transactions, because automated systems did not exist to systematically prevalidate them. DFAS was reluctant to manually prevalidate intergovernmental transactions because it would be time-consuming and would adversely affect the Department's ability to pay its bills in a timely manner. However, DFAS had not developed a plan to prevalidate OPAC transactions and other intergovernmental transactions. DFAS should develop a plan that includes milestones, performance measures, and expected backlogs. The dollar value of undistributed intergovernmental transactions that remain in suspense account F3885 for more than 60 days should be reported as unmatched disbursements.

Recommendation

We recommend that the Director, Defense Finance and Accounting Service, develop a plan for prevalidating On-Line Payment and Collection transactions as well as other types of intergovernmental transactions. The plan should identify specific milestones, performance measures, and expected backlogs.

Management Comments Required

The Defense Finance and Accounting Service did not comment on a draft of this report. We request that the Director, Defense Finance and Accounting Service, provide comments on the final report.

Appendix A. Audit Process

Scope

Work Performed. We reviewed the procedures for making and accounting for naval shipyard payments at DFAS Norfolk, Norfolk, Virginia, in August and September 2000. We reviewed vendor payments made using the Computerized Accounts Payable System and procedures for accounting for naval shipyard payments made via the OPAC system. In FY 2000, the net amount of OPAC payments and collections made by DoD disbursing stations totaled \$26.8 billion. We also reviewed DFAS plans for prevalidating disbursements and guidance for reporting OPAC transactions in suspense account F3885, Undistributed Intergovernmental Payments.

DoD-Wide Corporate-Level Government Performance and Results Act Goals. In response to the Government Performance and Results Act, the Secretary of Defense establishes DoD-wide corporate-level goals, subordinate performance goals, and performance measures. This report pertains to achievement of the following goal and subordinate performance goal.

FY 2001 Corporate-Level Goal 2: Prepare now for an uncertain future by pursuing a focused modernization effort that maintains U.S. qualitative superiority in key warfighting capabilities. Transform the force by exploiting the revolution in military affairs, and reengineer the Department to achieve a 21st century infrastructure. **(01-DoD-2)**

FY 2001 Subordinate Performance Goal 2.5: Improve DoD financial and information management. **(01-DoD-2.5)**

DoD Functional Area Reform Goals. Most DoD functional areas have also established performance improvement reform objectives and goals. This report pertains to achievement of the following functional area objective and goal.

Financial Management Area. Objective: Strengthen internal controls. **Goal:** Improve compliance with the Federal Managers' Financial Integrity Act. **(FM-5.3)**

General Accounting Office High-Risk Area. The General Accounting Office (GAO) identified several high-risk areas in DoD. This report provides coverage of the Defense Financial Management and Systems Modernization high-risk areas.

Methodology

To assess the procedures for making and accounting for naval shipyard payments at DFAS Norfolk, we reviewed guidance issued by DFAS and the Department of the Treasury, discussed procedures for making payments and

accounting for naval shipyard payments with DFAS Norfolk personnel, and reviewed selected transactions. We discussed the status of plans for prevalidating disbursements with DFAS Arlington personnel. We also reviewed DoD Regulation 7000.14-R, "DoD Financial Management Regulation," volume 3, chapter 11, "Unmatched Disbursements, Negative Unliquidated Obligations, In-Transit Disbursements, and Suspense Accounts," January 2001, for policy guidance on reporting problem disbursements and for using and reporting undistributed intergovernmental payments.

Use of Computer-Processed Data. We did not use computer-processed data to perform this audit.

Audit Type, Dates, and Standards. We performed this financial-related audit from July 2000 through March 2001 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD. We comply with Government Auditing Standards except for the requirement for an external quality control review. Measures have been taken to obtain an external quality control review.

Contacts During the Audit. We visited or contacted individuals and organizations within DoD. Further details are available on request.

Appendix B. Prior Coverage

During the last 5 years, GAO and the Inspector General, DoD, have issued numerous audit reports discussing issues related to the need to promptly match disbursements to corresponding detail obligations in accounting records and the problems that occurred when prevalidation was not performed.

General Accounting Office

GAO Report No. GAO/AIMD-00-10 (OSD Case No. 1919), "Increased Attention Needed to Prevent Billions in Improper Payments," October 29, 1999

GAO Report No. GAO/AIMD-99-19 (OSD Case No. 1642), "Problems in Accounting for Navy Transactions Impair Funds Control and Financial Reporting," January 19, 1999

GAO Report No. GAO/AIMD-97-59 (OSD Case No. 1316), "Improved Reporting Needed for DoD Problem Disbursements," May 1, 1997

GAO Report No. GAO/AIMD-96-82 (OSD Case No. 1149), "DoD Needs to Lower the Disbursement Prevalidation Threshold," June 11, 1996

Inspector General, DoD

Inspector General, DoD, Report No. 99-135, "Trends and Progress in Reducing Problem Disbursements and In-Transit Disbursements," April 16, 1999

Inspector General, DoD, Report No. 96-156, "Implementation of the DoD Plan to Match Disbursements to Obligations Prior to Payment," June 11, 1996

Appendix C. Allegation and Audit Results

Allegation. The Defense Hotline received an allegation that DFAS Norfolk stopped prevalidating payments for naval shipyards based on guidance from DFAS Arlington. By not prevalidating payments, the complainant stated that overpayments would occur and individuals and contractors would bill for goods and services not provided.

Audit Results. The allegation was not substantiated. DFAS Norfolk prevalidated commercial payments for naval shipyards. However, a program to prevalidate OPAC transactions never existed. In June 2000, DFAS Norfolk discontinued performing detailed reviews of the support for charges to funds of the naval shipyards by other governmental organizations before posting them to accounting records. DFAS Norfolk discontinued this practice because it was time-consuming and the Department of the Treasury issued new reporting procedures for unprocessed transactions between Federal agencies.

Past Practice. Prior to mid-1999, intergovernmental transactions were prevalidated similar to commercial payments. Subsequently, the Department of the Treasury's OPAC system was used to process most intergovernmental transactions. As part of that process, DFAS Norfolk performed detailed reviews of the support for charges to funds of the naval shipyards by other governmental organizations before posting them to accounting records, but after the payments were made. Accounts payable billing technicians at DFAS Norfolk prepared a NAVCOMPT Form 2277, "Voucher for Disbursement and/or Collection," for each OPAC transaction that it received from a disbursing office. The NAVCOMPT Form 2277 was sent to the accounts payable office at the appropriate naval shipyard. The accounts payable office verified that the charges were legitimate and validated that the appropriate line of funding was charged. Once the accounts payable office verified this information, the voucher and supporting documentation were routed to a supervisor for approval. DFAS Norfolk used this information to accept the OPAC transactions and post them to the accounting records. If problems were identified, such as the citation of an incorrect line of funding, or identification of a duplicate payment, the NAVCOMPT Form 2277 was returned to DFAS Norfolk. DFAS Norfolk personnel then rejected the transactions back to the disbursing office. DFAS Norfolk placed in a suspense account any transactions that were not cleared by the end of the month.

Revised Procedure. In June 2000, DFAS Norfolk stopped verifying the support for the payments with the naval shipyards before accepting the OPAC transactions. This practice stopped because of a change in policy that was aimed at reducing the number and dollar value of OPAC transactions in suspense accounts. The process of coordinating the OPAC transactions with the naval shipyards was time-consuming. It often took several days to perform the function. In June 2000, a DFAS Arlington employee in the Resource Management Directorate confirmed to DFAS Norfolk personnel that DFAS did not require the prevalidation of intergovernmental transactions.

Appendix D. Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)
Deputy Chief Financial Officer
Director for Accounting Policy
Deputy Comptroller (Program/Budget)

Department of the Army

Auditor General, Department of the Army

Department of the Navy

Naval Inspector General
Auditor General, Department of the Navy

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)
Auditor General, Department of the Air Force

Other Defense Organization

Director, Defense Finance and Accounting Service

Non-Defense Federal Organization

Office of Management and Budget

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs

Congressional Committees and Subcommittees, Chairman and Ranking Minority Member (cont'd)

House Committee on Appropriations

House Subcommittee on Defense, Committee on Appropriations

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House Subcommittee on Government Efficiency, Financial Management, and Intergovernmental Relations, Committee on Government Reform

House Subcommittee on National Security, Veterans Affairs, and International Relations, Committee on Government Reform

House Subcommittee on Technology and Procurement Policy, Committee on Government Reform

Audit Team Members

The Finance and Accounting Directorate, Office of the Assistant Inspector General for Auditing, DoD, prepared this report. Personnel of the Office of the Inspector General, DoD, who contributed to the report are listed below.

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